

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:MSR:KSM:KCY:TL-N-471-99
DPKensinger

date: **JAN 29 1999**

to: Director, Kansas City Service Center
P.O. Box 7905, Stop 4100, RA Unit, Annex 2
Shawnee Mission, Kansas 66207
Attn: Bridgette E. Dunmore

from: Assistant District Counsel, Kansas-Missouri District, Kansas City

subject: Application of Sequa Corporation Decision

[REDACTED]
Advisory Opinion - Significant

This refers to your request for advice with respect to the application of the decision in Sequa Corporation v. United States, 97-1 U.S.T.C. ¶ 50,317 (S.D.N.Y. 1996) to the payment of interest to the above-named taxpayer. Earlier we had provided you with a partial response but were unable to provide a complete response. We have now obtained additional information as well as the advice of the National Office on this situation. Consequently we can now give you a complete response.

DISCLOSURE STATEMENT

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Examination or Appeals recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

We will not repeat the facts from our prior memorandum dated September 18, 1998 but only summarize them briefly here. The taxpayer filed its income tax return for the period ended June 30, [REDACTED] on [REDACTED]; this return showed an overpayment in the total amount of \$ [REDACTED]. The overpayment was applied to the next fiscal year (the period ended June 30, [REDACTED]). The taxpayer, however, made estimated tax payments for the year ended June 30, [REDACTED], which fully paid the liability for that year.

Subsequently, the Service assessed a deficiency in the amount of \$ [REDACTED] on [REDACTED] the taxpayer paid this deficiency by an advance payment on [REDACTED]. The general issue is when interest begins to run on this deficiency. When we issued our earlier opinion we did not know the tax period to which this taxpayer actually applied the overpayment from fiscal [REDACTED]; nor did we know the position our National Office would take with respect to the application of Sequa to this situation.

The transcripts for the taxpayer's taxable years ended June 30, [REDACTED], [REDACTED], [REDACTED], [REDACTED], [REDACTED] and [REDACTED] show that the overpayment credits for fiscal [REDACTED] ([REDACTED]) were not used to pay estimated taxes for the tax years ended June 30, [REDACTED] and [REDACTED] ([REDACTED] and [REDACTED]). The estimated payments for fiscal [REDACTED] ([REDACTED]) were less than the total tax liability and, according to the transcript of account, a portion of the overpayment credit from fiscal [REDACTED] ([REDACTED]) was used to pay the tax for fiscal [REDACTED] ([REDACTED]) with a resulting overpayment of \$ [REDACTED] for fiscal [REDACTED]. That overpayment was applied to the estimated taxes for fiscal [REDACTED] ([REDACTED]). The estimated taxes for fiscal [REDACTED] were full paid and there was an overpayment from fiscal [REDACTED] which was applied to fiscal [REDACTED] ([REDACTED]). A portion of the overpayment credit from fiscal [REDACTED] ([REDACTED]) was used to satisfy the tax liability for fiscal [REDACTED] ([REDACTED]). There was an overpayment for fiscal [REDACTED] which was credited fiscal [REDACTED] ([REDACTED]). Thus, it appears that none of the overpayment from fiscal [REDACTED] ([REDACTED]) was needed to satisfy the estimated taxes for fiscal [REDACTED] ([REDACTED]), and that such overpayment credits were not used until the fiscal [REDACTED] ([REDACTED]) tax liability was partially satisfied by such credits. As noted below, however, it is the Service's position that even if the overpayment credit is not needed for the estimated taxes for the

subsequent tax year, the latest date on which interest will begin to accrue on the subsequently determined deficiency for the first year will be the due date of the return, without extension, for the second year, in this case fiscal [REDACTED] ([REDACTED]).

In general the government is entitled to interest on a deficiency in tax for the period that the tax was due and unpaid. I.R.C. § 6601(a); Avon Products v. United States, 588 F.2d 342 (2d Cir. 1978). If a deficiency in tax is determined after the taxpayer elected to credit a return overpayment against its estimated tax liability for the next succeeding year, interest will begin to accrue on the amount of the deficiency equal to the amount of the return overpayment as of the effective date of the credit elect. H.R. Rep. No. 98-432 (Part II), 98th Cong., 2d Sess. 1489-1490 (1984), reprinted in 1984 U.S.C.C.A.N. 1132-1133; see also, Rev. Rul. 88-98, 1988-2 C.B. 356. Section 413 of the Tax Reform Act of 1984 provides that overpayments of tax will be credited against the estimated income tax for the next succeeding year with full regard to Rev. Rul. 77-475, 1977-2 C.B. 476.

Rev. Rul. 77-475 provides the manner in which interest on a subsequently determined deficiency is computed under I.R.C. § 6601(a) when the taxpayer makes an election to apply an overpayment to the succeeding year's estimated taxes. When a taxpayer elects to apply an overpayment to the succeeding year's estimated taxes, the overpayment is applied to unpaid installments of estimated tax due on or after the date(s) the overpayment arose, in the order in which they are required to be paid to avoid an addition to tax for failure to pay estimated tax under I.R.C. § 6655 with respect to such year. However, in any case, the overpayment is a payment of the succeeding year's income tax liability no later than the due date (without regard to extensions) of the succeeding year's income tax return. Consequently, to the extent the overpayment is not needed to satisfy specific installments of estimated tax for the succeeding year's estimated tax, interest on the first year's deficiency begins to run from the original unextended due date of the succeeding year's income tax return.

In the instant case, the taxpayer's fiscal [REDACTED] ([REDACTED]) tax year does not fit within the fact pattern set forth in May Department Stores Co. v. United States, 96-2 U.S.T.C. ¶ 50,596

¹ In 1983 the Service revoked Rev. Rul. 77-475. However, in response to tremendous public criticism and expected Congressional action, the Service promulgated Rev. Rul. 84-58, 1984-1 C.B. 2564, which reinstated and modified Rev. Rul. 77-475 on March 30, 1984.

(Fed. Cl, 1996) because it had fully paid all of its installments of estimated tax for fiscal [REDACTED] ([REDACTED]) and, therefore, did not need any of the return overpayment from fiscal [REDACTED] ([REDACTED]) to pay the estimated tax for fiscal [REDACTED]. The recent case of Sequa, supra, stands for the proposition that interest on the deficiency for the first year would not begin to run where there has been no application of the overpayment to pay estimated taxes of subsequent tax years in order to avoid the addition to tax for failure to pay estimated taxes under I.R.C. § 6655, or the overpayment has not been refunded. Accordingly, the taxpayer in this case can argue, relying on the rationale of Sequa, that the Service has had the benefit of the fiscal [REDACTED] ([REDACTED]) overpayment from the time it was generated in fiscal [REDACTED] and interest will not begin to accrue on the subsequently determined deficiency for the year until such time as the overpayment is used by the taxpayer to pay estimated taxes in order to avoid the addition to tax for failure to pay estimated taxes under section 6655, which in this case is beyond the end of the fiscal [REDACTED] ([REDACTED]) year. However, as noted above, the Service disagrees with the Sequa decision and has taken the position that in all cases, the overpayment is a payment of the succeeding year's income tax liability no later than the due date (without regard to extensions) of the succeeding year's income tax return.

In summary, no part of the taxpayer's fiscal [REDACTED] ([REDACTED]) return overpayment was needed to avoid the addition to tax for failure to pay estimated income taxes in fiscal [REDACTED] ([REDACTED]). Therefore, interest on the subsequently determined deficiency for fiscal [REDACTED] ([REDACTED]) begins to run from the date on which the return overpayment is applied to the succeeding year's tax liability which will not be later than the unextended due date of the succeeding year's income tax return. In this instance the overpayment from fiscal [REDACTED] will be applied to the next year's liability on the unextended due date of the fiscal [REDACTED] ([REDACTED]) return and this date is [REDACTED]. Thus, interest on the deficiency for this taxpayer's fiscal [REDACTED] ([REDACTED]) deficiency will run from [REDACTED].

As no further action is required by this office we are closing our file. If you have any questions, contact the undersigned at (816)283-3046, ext. 164.

(Signed) Dale P. Kensinger

DALE P. KENSINGER

Assistant District Counsel

Office of Chief Counsel
Internal Revenue Service


memorandum

CC:MSR:KSM:KCY:TL-N-5886-98
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date: **SEP 18 1998**

to: Director, Kansas City Service Center
P.O. Box 24551
Kansas City, MO 64131
Attn: Bridgette E. Dunmore

from: Assistant District Counsel, Kansas-Missouri District, Kansas City

ject: Application of Sequa Corporation Decision


This refers to your request for advice concerning the application of the decision in Sequa Corporation v. United States, 97-1 U.S.T.C. ¶ 50,317 (S.D. N.Y. 1996) to the payment of interest to the above-named taxpayer. Because we do not have sufficient information we cannot provide you with a complete response now. We will, however, briefly discuss the situation and provide you with some general comments.

DISCLOSURE STATEMENT

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Examination Division or Appeals recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to the Examination Division, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on the Examination Division or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

The taxpayer filed its corporate income tax return for the taxable year ended June 30, [REDACTED] on [REDACTED] pursuant to an extension to file. The taxpayer reported a tax liability of \$ [REDACTED]. The taxpayer paid this liability with federal tax deposits and the application of overpayments from prior taxable years as set forth below.

Deposit/Application of Overpayment	Date	Amount
Overpayment Applied	[REDACTED]	\$ [REDACTED]
Overpayment Applied	[REDACTED]	[REDACTED]
Federal Tax Deposit	[REDACTED]	[REDACTED]
Federal Tax Deposit	[REDACTED]	[REDACTED]
Federal Tax Deposit	[REDACTED]	[REDACTED]
Federal Tax Deposit	[REDACTED]	[REDACTED]
Total		\$ [REDACTED]

The transcript shows the application of two overpayments on the date of [REDACTED] apparently because the source of the overpayments was different. The overpayment of \$ [REDACTED] was from fiscal [REDACTED] (the immediately preceding taxable period) and the overpayment of \$ [REDACTED] was from a period prior to the immediately preceding taxable period. The result was that the taxpayer had overpayments for its year ended June 30, [REDACTED], which were applied to the following taxable year (taxable year ended June 30, [REDACTED]). The amount of the overpayments applied to the taxable year ended June 30, [REDACTED] were in the amounts of \$ [REDACTED] and \$ [REDACTED], a total of \$ [REDACTED]. The date the overpayments were applied to the succeeding year was [REDACTED].

The Service assessed a deficiency in the amount of \$ [REDACTED] on [REDACTED] and the taxpayer paid this deficiency by an advance payment on [REDACTED]. The general issue is the date from which interest accrues with respect to an amount equal to the overpayments applied to fiscal [REDACTED].

The taxpayer contends that the Service should not charge interest from [REDACTED] because the taxpayer had fully paid its estimated tax liability for the succeeding taxable year with payments other than the application of the overpayment from the taxable year ended June 30, [REDACTED]. From the information available, we do not know what date the taxpayer thinks the Service should properly charge interest. The taxpayer relies on the decision in Segua, supra, as authority for its position.

In Sequa, supra, the taxpayer had filed its corporate income tax return for 1990 on September 15, 1991 pursuant to an extension. The return reported a liability of \$11.1 million and total payments of about \$19.8 million. The result was an overpayment of \$8.7 million. Sequa elected to apply this overpayment to its tax liability for 1991. On August 14, 1992 Sequa filed an amended 1990 tax return reporting an additional tax liability in the amount of \$1.7 million and this reduced Sequa's actual overpayment to about \$7 million.

The Service informed Sequa that it would apply \$1.7 million from the funds representing Sequa's 1990 overpayment which had not been needed to satisfy Sequa's tax liability for 1991. The Service also charged interest with respect to the additional \$1.7 million from March 15, 1991, the date Sequa's 1990 tax was due, until March 15, 1992, which is the date Sequa's 1991 tax was due and according to the Service, the date the overpayment from 1990 became available to satisfy the additional tax liability reported by Sequa on the amended return for 1990. In other words, the Service took the position that when the overpayment reported on the original return filed by Sequa was applied to the liability for 1991, the overpayment was not available to apply to the additional liability for 1990 reported on the amended return until the due date of Sequa's return for 1991 at which time Sequa's liability would be known and an overpayment for 1991 could be determined.

The court held that the Service had improperly charged interest from the due date of the return for 1990 (March 15, 1991) to the due date of the return for 1991 (March 15, 1992). The court first looked at the period March 15, 1991 to September 15, 1991, the date Sequa filed its return for 1990. The court concluded that Sequa had paid in full its liability for 1990, including the additional liability reported on the amended return, by March 15, 1991. Thus, during this period there was no tax which both due and unpaid. For that reason the Service had no authority to charge interest during the period March 15, 1991 to September 15, 1991.

For the period from September 15, 1991 to March 15, 1992 the court also concluded that the Service had no authority to charge interest. The court looked to the status of the taxpayer's account for 1991 and determined that the taxpayer had paid sufficient estimated tax payments for 1991 to satisfy its tax liability for 1991 without taking into account the application of the overpayment from 1990 to 1991, which the taxpayer elected on its 1990 return. Because Sequa had paid sufficient estimated tax payments for 1991 to satisfy its liability for 1991 without considering the overpayment from 1990, the court stated that the Service never lost the use of the money as a payment of Sequa's 1990 liability. As interest is a payment for the use of money, the Service had no

basis for charging interest during the period September 15, 1991 to March 15, 1992.

We have been informally advised that the Service will not litigate future cases which are indistinguishable from Sequa. We cannot determine, however, from the information which we now have whether the instant situation is controlled by Sequa. Specifically, we do not have the transcripts of account of this taxpayer for the taxable period subsequent to the period ended June 30, [REDACTED]. Thus, we cannot determine when, if ever, the overpayment from fiscal [REDACTED] was necessary to satisfy the liability for fiscal [REDACTED] or some subsequent year. Since the deficiency for this taxpayer's liability for the period ended June 30, [REDACTED] was not paid until [REDACTED], this taxpayer may have used the overpayment from fiscal [REDACTED] to satisfy its tax liability for any number of intervening taxable periods. In fact, we infer that at some point the overpayment from fiscal [REDACTED] was applied to a later liability because in [REDACTED] the taxpayer paid the entire deficiency without reducing the payment by the amount of the overpayments applied to the fiscal [REDACTED] tax liability on [REDACTED]. The taxpayer in its correspondence with the service center does not state when it believes interest with respect to the amount of the applied overpayment should begin to accrue; it simply states that interest should not accrue from [REDACTED], the date the Service applied the overpayments from fiscal [REDACTED] to the succeeding year (year ended June 30, [REDACTED]). If you can provide us with transcripts for the taxable periods after [REDACTED] we can determine if Sequa applies.

We emphasize that this issue relates to interest on only the portion of the deficiency which could be satisfied by the application of the overpayment reported on the original return, not the entire deficiency. Although not specifically stated in the request for advice, we assume that this taxpayer agrees to pay interest from the due date of the fiscal [REDACTED] return ([REDACTED]) until the date of payment to the extent the deficiency exceeds the overpayments applied to the fiscal [REDACTED] account on [REDACTED]. Section 6601(a) provides for interest from the date prescribed for payment until the date of payment. Section 6151(a) provides that tax shown on a return shall be paid "at the time and place fixed for filing the return (determined without regard to an extension of time for filing the return)." Thus, the time for paying the tax is the original due date of the return, or [REDACTED] in this instance. Pursuant to section 6601(a), therefore, this taxpayer is liable for interest on the portion of the deficiency not satisfied by the overpayments applied to the fiscal [REDACTED] account from [REDACTED] until payment on [REDACTED].

As no further action by this office is possible until transcripts for the intervening taxable periods are obtained, we are currently closing our file. As soon as you obtain transcripts, however, forward them to us and we will provide you with our opinion on the period during which interest accrues with respect to the portion of the deficiency equal to the overpayment reported on the fiscal [REDACTED] return. If you have any questions, contact the undersigned at (816) 283-3046, ext. 164.

(Signed) Dale P. Kensinger

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